

GMP equalisation – an answer at last

The High Court has [held](#) that schemes are required to equalise benefits for the effect of guaranteed minimum pensions (“GMPs”). The Court also considered a number of possible equalisation methods. It held that the employer could require the trustees to adopt the lowest cost method.

Background

GMPs are a minimum benefit that schemes that were contracted-out on a salary-related basis between 1978 and 1997 are required to provide. The rules governing the accrual and payment of GMPs are set out in legislation. Those rules differ as between men and women in a number of respects – in particular, GMPs are payable at age 60 for women and age 65 for men.

Starting with *Barber* in 1990, a series of court decisions have established the broad principle that occupational pensions earned from 17 May 1990 must be equal for men and women. However, another series of court decisions have established that state pensions do not have to be equal for men and women.

Until now, it has not been clear whether:

- benefits must also be equalised for the effect of unequal GMPs (since GMPs are a replacement for a state pension benefit); or
- if benefits must be equalised, how this should be achieved (since the question of which sex has the higher overall benefit will differ from one case to another and may change over an individual’s lifetime).

The equalisation requirement and equalisation methods

The Court concluded that trustees are under a duty to equalise benefits for the effect of GMPs. The Court also considered various possible equalisation methods. In assessing the methods, the Court looked at (a)

whether they achieved equalisation, and (b) whether they complied with the principle of minimum interference. This principle requires that, where there is more than one way of providing equal benefits, the option chosen should be the one that involves the least interference with the rights of any party.

The Court held that all but one of the suggested methods achieved equalisation, but that the employer could require the trustees to adopt the cheapest method (“**Method C2**”) on the basis of the principle of minimum interference. Method C2 involved providing the better of a male or female comparator pension each year, subject to a process offsetting accumulated prior gains and making an allowance for interest on those accumulated gains. The Court also concluded that a variation on Method C2, whereby the GMPs would be equalised and then converted into ordinary scheme benefits, could be adopted, but would require the employer’s consent under the GMP conversion legislation.

Past underpayments

The Court held that trustees are obliged not only to correct future benefit payments, but also past underpayments. The Court considered whether any limitation period would apply to past underpayments and concluded that:

- there is no statutory limitation period; but
- where the scheme rules contain a provision under which unclaimed pension instalments are forfeited after six years, that provision may be enforceable – this will depend on the wording of the rule in question.

In addition, the Court held that any arrears of payments should be paid with interest at 1% over base rate.

Implications for schemes

Clearly, this ruling has significant implications for schemes that were contracted-out on a salary-related basis between 1978 and 1997. GMP equalisation will be a complicated and costly process – both in terms of the additional scheme liabilities created and the administration costs – and will take time to plan and implement.

However, it is important to note that the ruling may be appealed. Several issues also remain undecided by the Court, such as the treatment of past transfers-out, and some of these issues may be the subject of a further Court hearing. The government previously consulted on various matters relating to GMP equalisation and halted this work pending the outcome of this case, but should now resume its work in this area. Therefore there may well be future developments which affect the extent to which, and the way in which, schemes are required to comply with the equalisation requirement.

In light of this, we suggest that trustees and employers should adopt a three stage approach to responding to the decision:

1. Immediate actions

- *Member communications* – trustees should consider whether to send a general communication to members about the ruling explaining that (a) GMP equalisation is now required, but will take some time to implement, and (b) the process undertaken may be affected by future developments such as an appeal.
- *Transfers-out* – trustees should consider whether adjustments can be made to the cash equivalent transfer value basis in the interim which will ensure that the transfer is compliant. Otherwise, trustees should include a similar statement in transfer packs warning members that schemes are now required to equalise benefits for the effect of GMPs and that once the equalisation process is complete, their benefits may be higher than the current transfer value, but the transfer may not be revisited.
- *Retirement quotations* – trustees should include a similar statement in retirement quotations noting that schemes are now required to equalise benefits for the effect of GMPs and that once the equalisation process is complete, their benefits may be adjusted.

- *Commutations* – trustees should consider what policy to adopt in relation to trivial and small pot commutations.
- *Valuations* – trustees and employers should consider the impact of the equalisation requirement on current valuations.
- *Forfeiture rules* – trustees should seek legal advice on the extent to which their scheme rules operate to impose a limit on the period for which past underpayments must be corrected. Depending on this advice, trustees may need to reconsider their approach to the payment of arrears in respect of all benefits, not just GMPs.
- *Accounting treatment* – employers should consider the impact of the equalisation requirement on their accounting position.

2. GMP reconciliation

Trustees should complete their GMP reconciliation process before moving onto a GMP equalisation process.

3. GMP equalisation

Once the GMP reconciliation process has been completed, and there is more clarity on whether the ruling will be appealed and on any government action in light of the ruling, trustees should plan and implement a GMP equalisation process, in consultation with the employer. Ideally this process should also incorporate any rectifications to GMPs required as a result of the GMP reconciliation process. The trustees and the employer may also want to consider converting GMPs into ordinary scheme benefits as a final step in the process.

If you have any questions about the issues raised in this legal update, please contact your usual Mayer Brown contact or:

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